No. 98-1271

Supreme Court, U.S.
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IN THE

# Supreme Court of the United States

OCTOBER TERM, 1998

JOHN ROMANO,

*Petitioner,*

—v.—

SECURITIES AND EXCHANGE COMMISSION,

*Respondent.*

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

## REPLY BRIEF FOR PETITIONER

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## QUESTIONS PRESENTED

1. Is manipulative intent or purpose an essential element of a claim of primary liability for market manipulation under Section 10(b) of the Securities Exchange Act of 1934?

2. Does recklessness satisfy the scienter requirement for imposition of primary liability for market manipulation under Section 10(b) of the Securities Exchange Act of 1934?

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## REPLY BRIEF FOR PETITIONER

### STATEMENT

Petitioner John Romano ("Romano") submits this reply brief in support of his Petition for a Writ of Certiorari to review the judgment of the United States Court of Appeals for the Second Circuit. The Court of Appeals reversed the memorandum order dismissing the claim of market manipulation against Romano issued by the United States District Court for the Southern District of New York. As fully set forth in the Petition, this case presents important questions concerning the essential elements of a claim of primary liability for market manipulation under Section 10(b) of the Securities Exchange Act of 1934.

Relying on the meaning of the term manipulation as defined in decisions of the Supreme Court of the United States, the district court ruled that manipulative intent, not mere knowledge or recklessness, was required. Accordingly, the district court dismissed the market manipulation claim against the trader Romano because the Amended Complaint alleged that in effecting the trades prearranged by the stock promoters Romano acted knowingly or recklessly, but did not allege that he acted with a manipulative intent. Pet. App. 19a-20a, 25a.

In its decision reversing the district court, the Second Circuit Court of Appeals ruled that a stock trader may be held primarily liable for manipulation of the market even though the trader did not act with a manipulative purpose or intent and did not share the manipulative purpose or intent of the principal defendants, the stock promoters. The Court of Appeals reached this rather remarkable conclusion without citing a single case holding that manipulative purpose or intent is not an essential element of a manipulation claim, and without addressing the decisions by this Court that belie the proposition that a person may be liable for market manipulation without regard to manipulative intent or purpose. The Court of Appeals ruled alternatively that knowledge or recklessness constituted sufficient scienter to state a claim of liability under § 10(b) for market manipulation. Pet. App. 3a, 7a, 9a-10a.

Respondent Securities and Exchange Commission ("SEC") has submitted a brief in opposition to the Petition. However, as we show below, the arguments made in respondent's brief in opposition are without merit.

## ARGUMENT

1. Respondent SEC argues that the petition for a writ of certiorari should be denied because the decision of the Court of Appeals is interlocutory. Respondent asserts that "[e]xcept in extraordinary circumstances not present here, this Court's

practice is to decline to exercise certiorari jurisdiction over cases that are in an interlocutory posture." Respondent's Brief, at pp.7-8. This argument is of no avail here for several reasons.

First, this is an interlocutory appeal pursuant to the provisions of 28 U.S.C. § 1292(b). The district court certified its order for interlocutory review on the ground that the order "involves a controlling question of law as to which there is substantial ground for difference of opinion and that an immediate appeal from the order may materially advance the ultimate termination of the litigation," 28 U.S.C. § 1292(b). Pet. App. 24a-26a. And the Second Circuit Court of Appeals exercised its discretion under § 1292(b) to hear and decide the interlocutory appeal. Contrary to respondent's suggestion, this "Court regularly reviews cases decided in the courts of appeals on appeal under 28 U.S.C.A. § 1292(b) without further comment on its own jurisdiction. [citing numerous cases]." Wright, Miller & Cooper, *Federal Practice and Procedure: Jurisdiction 2d* § 4036, at pp. 28-29, n.50(2d Ed. 1988), and Supp., at p. 8 (1999).

Second, respondent's argument ignores the nature of the issues presented here. As the district court stated in certifying the order for interlocutory review, this appeal involves the "important" and "controlling" question of law as to "what level of scienter is required before a person trading in securities can be said to manipulate the securities". Pet. App. 25a. As the district court further stated in its certification for interlocutory appeal:

> The Amended Complaint alleged knowledge or recklessness on the part of defendant Romano, whereas this Court has ruled that intent was required before a trade could be designated manipulative. . . . Specifically, the Court . . . has ruled that where, as here, manipulation is the basis of the claim, manipulative intent, and not mere

> knowledge or recklessness, is required before Rule 10b-5 is violated.

Pet. App. 25a.

Thus, the issue here as to the requisite level of scienter (whether specific intent to manipulate, knowledge, or recklessness) clearly involves an important and clear-cut issue of law. Moreover, that issue of law is controlling and fundamental to the further conduct of this case. Pet. App. 25a-26a. Manifestly, that is the situation where, as here, the critical manipulation claim against Romano was dismissed by the district court, and the ruling of the court of appeals has reversed the dismissal and required further proceedings on the claim in the district court. See Wright, Miller & Cooper, *Federal Practice and Procedure: Jurisdiction 2d* § 4036, *supra*, at pp. 30-32, and n.57.

Third, the SEC's argument concerning the interlocutory posture of the case is substantially undermined by the position that it took in the Brief For The United States As *Amicus Curiae* filed in this Court on petition for a writ of certiorari in *Central Bank of Denver, N.A. v. First Interstate Bank of Denver, N.A.*, No. 92-854 (October Term 1992). In *Central Bank*, the Tenth Circuit Court of Appeals had held that recklessness was sufficient scienter to hold a secondary actor liable for aiding and abetting the primary violator. *See Central Bank of Denver, N.A. v. First Interstate Bank of Denver, N.A.*, 511 U.S. 164, 168-69, 114 S.Ct. 1439, 1443-44 (1994). This Court invited the Solicitor General to express the views of the United States on petition for a writ of certiorari. That petition also involved interlocutory review: the Court of Appeals had reversed the decision of the district court granting summary judgment dismissing the aiding and abetting claim against Central Bank. *Id.*

Although the government believed that the Court of Appeals' decision was correct, it agreed with petitioner Central Bank that the scienter issue warranted review by this

Court. With respect to the interlocutory aspect of the appeal, the government took a position that is at odds with the "exceptional circumstances" position enunciated in the case at bar. The government's brief stated:

> We recognize that the interlocutory nature of the decision below militates against immediate review by this Court. *See, e.g., Brotherhood of Locomotive Firemen v. Bangor & A.R.R.*, 389 U.S. 327, 328 (1967) (per curiam); *Hamilton-Brown Shoe Co. v. Wolf Bros. & Co.*, 240 U.S. 251, 258 (1916); *American Construction Co. v. Jacksonville, T. & K.W. Ry.*, 148 U.S. 372, 384 (1893). Nonetheless, it is well-established that "where * * * there is some important and clear-cut issue of law that is fundamental to the further conduct of the case and that would otherwise qualify as a basis for certiorari, the case may be reviewed despite its interlocutory status." R. Stern, E. Gressman & S. Shapiro, *Supreme Court Practice* 225 (6th ed. 1986) (citing cases). The issue of law presented in this case is not likely to be sharpened by factual elaboration at trial, and the question is clearly one that would otherwise qualify as a basis for certiorari.

Brief For The United States As *Amicus Curiae*, at pp. 17-18. And as noted in Romano's Petition, at p. 15, this Court granted certiorari to review two important questions presented (including the scienter issue), and decided the case without reaching the scienter question because it held that a private plaintiff may not maintain an aiding and abetting claim under Section 10(b).[1]

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[1] Respondent argues in footnote 3 of its brief that the second question presented in Romano's Petition (whether recklessness satisfies the scienter requirement for imposition of primary liability for market manipulation) is not properly presented for this Court's review because the statement by the Court of Appeals that recklessness is sufficient was only a "remark" or "observation" that it was not relying on for its decision. Respondent is mistaken. While the Court of Appeals concluded its opinion with a few "observations", Pet. App. 12a, the ruling concerning recklessness was in a prior part of the opinion. Pet. App. 10a. Moreover, although commenting that "we need not rely on this point," *id.*, the Court

2. Respondent SEC is also less than forthright with respect to the conflict between the decision of the Court of Appeals (namely, that petitioner Romano can be held liable on the market manipulation claim as a primary violator for effecting the stock promoters' trades if he had knowledge that the stock promoters intended to manipulate the market, even if he himself did not have or share that manipulative intent), and prior decisions of this Court. As shown in Romano's Petition, at pp. 12-13, those Supreme Court decisions make it clear that manipulation is a term of art that requires a specific intent to manipulate market activity or the price of securities. *Santa Fe Industries, Inc. v. Green*, 430 U.S. 462, 476, 97 S.Ct. 1292, 1302 (1977) (trading practices "that are intended to mislead investors by artificially affecting market activity"); *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 199, 96 S.Ct. 1375, 1384 (1976) ("intentional or willful conduct designed to deceive or defraud investors by controlling or artificially affecting the price of securities").

Respondent appears to argue that the Court of Appeals' decision that the secondary actor Romano can be held liable without a specific intent to manipulate does not conflict with this Court's decisions because the stock promoters are alleged to have acted with the requisite specific intent to manipulate market activity and the prices of securities. However, respondents do not offer any rationale to support the argument that

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of Appeals proceeded to decide the point: "we also note that the complaint's claim that Romano recklessly participated in the manipulation also alleges sufficient scienter. [Citations omitted.]" Pet. App. 10a. *See Oklahoma Tax Commission v. Citizen Band Potawatomi Indian Tribe of Oklahoma*, 498 U.S. 505, 512, 111 S.Ct. 905, 911 (1991) (Supreme Court proceeds to decide question of sovereign immunity after commenting that "[w]hile neither of these courts [district court and court of appeals] need have reached that question, they both did"). Respondent's citation of *Black v. Cutter Laboratories*, 351 U.S. 292, 297, 76 S.Ct. 824, 827 (1956) is inapposite because it involves a state court decision, review of which is not undertaken where the judgment rests on an independent state ground. *Id.* ("we should not pass on federal questions discussed in the opinion where it appears that the judgment rests on adequate state grounds").

a secondary actor can be held liable as a primary violator with a lesser scienter requirement (knowledge or recklessness) than is applicable to the primary actor (specific intent to manipulate); the *Santa Fe Industries* and *Ernst & Ernst* decisions of this Court provide no support for such a distinction; and the argument that the intent to manipulate requirement of primary liability can be dispensed with for a secondary actor is belied by the decision of this Court in *Central Bank* (a secondary actor who employs a manipulative device may be liable as a primary violator, assuming *"all* of the requirements for primary liability under Rule 10b-5 are met", 511 U.S. at 191, 114 S.Ct. at 1455).

## CONCLUSION

The petition for a writ of certiorari should be granted.

Dated: April 28, 1999

Respectfully submitted,

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